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No. _____

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In the Supreme Court of the United States

October Term, 1980

CHARLES REYNOLDS and LOIS A. REYNOLDS, his wife, as individuals and as parents and next friends of STEVEN REYNOLDS, and STEVEN REYNOLDS, individually,
Petitioners,

vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTION PRESENTED

The Federal Tort Claims Act provides for liability of the United States in the same manner and to the same extent as a private individual under like circumstances. The Act provides, however, that liability shall not apply to any claim arising out of misrepresentation.

The question presented is whether the "misrepresentation exception" to liability applies to a cause of action for personal injury (brain damage from asphyxiation) based upon negligent performance by the FmHA of a safety inspection in which defective installation of a furnace system was not discovered.

TABLE OF CONTENTS

PAGE

Question Presented 1
Opinion Below 3
Jurisdiction 3
Statutory Provisions Involved 3
Statement of the Case 3
Reasons Relied on for Allowance of the Writ 4

Appendices —

A. Opinion of Court of Appeals ..... App. 1
B. Opinion in *Neal v. Bergland*, No. 80-1278, 6th Cir, May 1, 1981 ..... App. 11

TABLE OF AUTHORITIES

Cases

Ausland v. United States, 488 F. Supp. 426 (N.D. S.Dak. 1980) ... 8
Hall v. United States, 274 F.2d 69 (10th Cir. 1959) 8
Hicks v. United States, 511 F.2d 407 (D.C. Cir. 1975) 8
Marival, Inc. V. Planes, Inc., 306 F.Supp. 855 (N.D. Ga. 1969) ... 8
Melton v. United States, 488 F.Supp. 1066 (D. D.C. 1980) ... 8
Moon v. Takisaki, 501 F.2d 389 (9th Cir. 1974) 8
Neal v. Bergland, No. 80-1278, 6th Cir., May 1, 1981 7
Saxton v. United States, 456 F2.d 1105 (8th Cir. 1972) 8
United Scottish Ins. Co. v. United States, 614 F.2d 188 (9th Cir. 1979) 8
United States v. Neustadt, 366 U.S. 696 (1961) ..... 4, et. seq.

Statutes and Regulations

28 U.S.C. §1346(b) 3
28 U.S.C. §2674 3
28 U.S.C. §2680(h) 4, 5
7 C.F.R. §1802.2(b) 5
7 C.F.R. §1804.3(d)(1) 5
7 C.F.R. §1804.4(g)(3) 5
7 C.F.R. §1822.2 5

OPINION BELOW

The opinion delivered in the Court of Appeals is officially reported at 643 F.2d 707 (10th Cir. 1981), and appears in the appendices hereto at App. 1. There was no opinion delivered in the District Court.

JURISDICTION

The judgment and opinion of the Court of Appeals was entered March 9, 1981. This Court has jurisdiction under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

The Federal Tort Claims Act provides, in relevant part, that:

> The United States shall be liable, respecting the provisions of this title relating to tort claims, in the same manner and to the same extent as a private individual under like circumstances . . . .

28 U.S.C. §2674. This provision for liability, however, "shall not apply to —

> (h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights.

28 U.S.C. §2680.

STATEMENT OF THE CASE

This is an action filed by plaintiffs in the United States District Court for the District of New Mexico for personal injury caused by the negligent or wrongful act or omission of an employee of the government, the basis for federal jurisdiction being 28 U.S.C. §1346(b). Plaintiff Steven Reynolds sustained serious brain damage by carbon monoxide poisoning from a defectively installed furnace in a new home which he was safekeeping for the owners, who were temporarily absent. The material allegations of plaintiffs' complaint are that the county supervisor of the Farmers Home Administration (FmHA) undertook, pursuant to statutory and regulatory obligations, a safety inspection of the newly constructed home. The FmHA performed the safety inspection in a negligent manner, in failing to discover that a natural gas furnace was installed without conversion for liquified petroleum gas. The statute and regulation imposing the inspection obligataion on FmHA has the safety of persons such as the claimant as an objective.

The United States moved for judgment on the pleadings, and the court, concluding that the FmHA owed no duty to inspect for safety to plaintiff, granted the defendant's motion. The Court of Appeals first considered whether the United States owed a tort duty of ordinary care to its borrowers' invitee to inspect for and disapprove unsafe conditions existing in the residential structure pursuant to FmHA mortgage loan procedures. The Court recognized that New Mexico subscribes to the common law liability of an actor who negligently undertakes to render services for or on behalf of a second party for the protection of a third party. The Housing Act of 1949 and applicable regulations were cited by the Court for the fact that safe housing is an objective of the Act, relevant regulations, and the specific inspections undertaken in this case. The Court held, however, "that the claim asserted by the plaintiffs-appellants in the instant case arises out of misrepresentation by the FmHA and is, accordingly, not actionable under the 'misrepresentation' exception contained in §2680(h) of the Federal Tort Claims Act."

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

IT IS UNSETTLED WHETHER THE "MISREPRESENTATION" EXCEPTION TO THE TORT CLAIMS ACT APPLIES WHEN GOVERNMENT LIABILITY IS BASED UPON FAILURE TO EXERCISE REASONABLE CARE WHILE MAKING A SAFETY INSPECTION PRESCRIBED BY STATUTE AND REGULATION

In the twenty years since the United States Supreme Court addressed the misrepresentation exception in *United States v. Neustadt*, 366 U.S. 696 (1961), substantial confusion has arisen in the lower federal courts over application of the exception where harm has been caused by failure of the government to exercise reasonable care while making a safety inspection prescribed by statute or regulation. Underlying the importance of this question is the pervasive involvement of the federal government in regulating safety in the private sector.

A. THE DECISION OF THE COURT OF APPEALS CONFLICTS WITH THE CONCEPT OF MISREPRESENTATION AS ARTICULATED BY THIS COURT

In *United States v. Neustadt, supra*, plaintiffs purchased a house with a private mortgage loan insured by the Federal Housing Administration (FHA) and, in determining whether the house was eligible for FHA mortgage insurance, the FHA had made an inspection and assigned an appraised value to establish the maximum amount of mortgage insurance obtainable. Plaintiffs sued the FHA for their economic loss, claiming they relied to their detriment on an excessive FHA appraisal, which had missed a defective foundation. In applying the misrepresentation exception of 28 U.S.C. §2680(h), the Supreme Court found that the government's duty was to use due care in obtaining and communicating information upon which a party may reasonably be expected to rely in the conduct of his economic affairs. A breach of that duty was held only to state the traditional and commonly understood legal definition of the tort of "negligent misrepresentation." 366 U.S. at 706.

Contrary to the conclusion of the Court of Appeals, *Neustadt* does not require dismissal of plaintiffs' claim. The Court of Appeals has confused (a) the duty to obtain and communicate information reasonably expected to be relied upon by others in the conduct of economic affairs, with (b) a duty to assist persons who live in rural areas to obtain safe dwellings. The Court has confused the negligent misrepresentation arising out of a breach of the former duty with the negligent performance of an operational task arising out of the breach of the latter duty.

As acknowledged by the Court of Appeals in its judgment and opinion, the basic objective of the FmHA in making rural housing loans is to assist persons who live in rural areas to obtain decent, safe, and sanitary dwellings, 7 C.F.R. §1822.2, and the primary objectives of supervision include assistance to such families to obtain safe housing. 7 C.F.R. §1802.2(b). New buildings are to conform with good construction practices and to applicable laws, ordinances, codes, and regulations which relate to safety, 7 C.F.R. §1804.3(d)(1), and the county supervisor is to inspect development work as frequently as necessary to assure that construction conforms with the plans and specifications. 7 C.F.R. §1804.4(g)(3). The misrepresentation exception, as construed by *Neustadt*, is erroneously extended by the Court of Appeals to the duty to use due care in operational tasks of inspections to assure statutory and regulatory objectives of safe housing.

This Court, in *Neustadt*, clearly drew a distinction between governmental activities which invade financial or commercial interests and governmental activities which invade other personal interests. *Neustadt* made it clear that the misrepresentation exception was not properly extended to the latter category of invasions, irrespective of categorical labels:

> Our conclusion neither conflicts with nor impairs the authority of Indian Towing Co. v. United States, 350 U.S. 61, 76 S.Ct. 122, 100 L.Ed. 48, which held cognizable a Torts Act claim for property damages suffered when a vessel ran aground as a result of the Coast Guard's allegedly negligent failure to maintain the beacon lamp in a lighthouse. Such a claim does not "arise out of * * * misrepresentation," any more than does one based upon a motor vehicle operator's negligence in giving a misleading turn signal. As Dean Prosser has observed, many familiar forms of negligent conduct may be said to involve an element of "misrepresentation," in the generic sense of that word, but "[s]o far as misrepresentation has been treated as giving rise in and of itself to a distinct cause of action in tort, it has been identified with the common law action of deceit," and has been confined "very largely to the invasion of interests of a financial or commercial character, in the course of business dealings." Prosser, Torts, §85, "Remedies for Misrepresentation," at 702-703 (1941 ed.). See also 2 Harper and James, Torts, §29.13, at 1655 (1956).

366 U.S. at 711, n. 26. The decision of the Court of Appeals clearly is in conflict with *Neustadt*.

B. THE DECISION OF THE COURT OF APPEALS IS IN CONFLICT WITH DECISIONS OF OTHER COURTS OF APPEALS ON THE QUESTION OF THE APPLICABILITY OF THE MISREPRESENTATION EXCEPTION

In *Neal v. Bergland*, No. 80-1278, 6th Cir., May 1, 1981, appearing in the appendices hereto at App.11,[1] the plaintiff had received a direct rural housing loan from the FmHA and eventually brought suit, including a tort claim, against the FmHA to pay for correcting the heating system and other construction defects in the house. The tort claim was based upon the same principle expressed in the Restatement

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[1]Petitioner is informed and believes that it is the intention of the United States to petition for a writ of certiorari to review the judgment and opinion of the United States Court of Appeals for the Sixth Circuit in *Neal v. Bergland, supra.*

(Second) of Torts as was the tort claim of Reynolds in the instant case. The opinion in *Neal* specifically refers to the decision in the instant *Reynolds* case " which appears to be contrary to our holding above. Careful review suggests that we take a different view of Congressional intent and the purposes of the statute with regard to technical assistance." *Neal v. Bergland, supra*, at n. 7. The holding of the Sixth Circuit which is contrary to the Tenth Circuit is expressed in the following language of the court:

> Plaintiff's claim, as we read it, is based not on misrepresentation, as in the issuance of a false or inaccurate appraisal report, but rather on FmHA's failure to use due care in a voluntary undertaking, i.e., inspection and supervision of the construction of her house. Congress, we believe, intended plaintiff to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the Act and plaintiff's particular circumstances.
>
> . . . .
>
> There is nothing in the amended complaint or in the facts and circumstances here present which lead to the conclusion that the kind of misrepresentation, as was found in *Neustadt* and as is specifically excluded under §2680(h) of the Federal Tort Claims Act, is the basis of plaintiff's claim. What plaintiff is complaining of is that FmHA negligently supervised construction and negligently inspected her house.

Nuestadt made applicability of the mispresentation exception clear where the ultimate objective of the government's activity was a representation of a financial or commercial character in the course of business dealings. *Neustadt* made inapplicability of the exception clear where the "misrepresentation" was, incidentally, no more than a misleading "signal" about unreasonable risks of harm from activities of the agency conducted under a statute or regulation having an objective other than obtaining and communicating information.

Neustadt, however, did not deal directly with the problem with which the courts have wrestled in noticeably increasing confusion over the past 20 years. This is the problem of tort claims based upon negligently conducted safety inspection and supervision which, incidentally, result in misrepresentations that unsafe structures, aircraft, products and services can be relied upon by the public as having met accepted safety standards of the government.

The discretionary function exception serves to decide many cases in which this problem arises. In groping for a key to the application of the misrepresentation exception, however, the opinions outside of the FHA appraisal cases seem simply to emphasize the misrepresentation

as a premise for denying liability, while emphasizing the "operational task" as a premise for establishing liability. Conflicting results in the courts of appeals are beyond rational distinction. *Compare* the Tenth Circuit opinion in *Reynolds v. United States, supra, with Hicks v. United States,* 511 F.2d 407 (D.C. Cir. 1975). *Compare Ausland v. United States,* 488 F.Supp. 426 (N.D. S.Dak. 1980), *with Hall v. United States,* 274 F.2d 69 (10th Cir. 1959), and *Saxton v. United States,* 456 F.2d 1105 (8th Cir. 1972). *Compare* the Sixth Circuit opinion in *Neal v. Bergland, supra,* and *Melton V. United States,* 488 F.Supp. 1066 (D. D. C. 1980), *with Moon v. Takisaki,* 501 F.2d 389 (9th Cir. 1974). *Compare United Scottish Ins. Co. v. United States,* 614 F.2d 188 (9th Cir. 1979), *with Marival, Inc. v. Planes, Inc.,* 306 F.Supp. 855 (N.D. Ga. 1969).

Petitioners respectfully submit that a proper question is whether the statute or regulation under which the agency of government has acted has as its objective a representation of fact to the person claiming to have been wronged; or, whether the statute or regulation has as its objective a safeguarding of the person or property of the claimant, with representations being only incidental to that objective.

The objective of the inspections required of the FmHA county supervisor in *Reynolds* was to assure that construction conformed with plans and specifications for safe housing. The risk of harm to the claimant was increased by the government's failure to exercise reasonable care to discover the defectively installed furnace. The resulting tacit representations of safety were only incidental to the operational task which was negligently performed. The Court of Appeals was in error in applying the misrepresentation exception.

Sufficent time has elapsed since this Court's decision in *Neustadt* and a sufficient body of case law has developed so that the contours of the various approaches taken by the lower federal courts on this question and the policies underlying those approaches are readily discernible. Transcending the erroneous application of the misrepresentation exception to petitioners' claim, and the substantial injustice done thereby, petitioners respectfully suggest that the long-standing and widespread confusion within the lower federal courts is creating general injustice which must be rectified.

While petitioners are prepared to argue that the proper resolution of the issue will result in a reversal of the decision of the Court of Appeals, petitioners respectfully submit that a definite resolution of the confusion, irrespective of the result, is of equal importance.

Respectfully submitted,

RICHARD E. RANSOM
Attorney for Petitioner

APPENDIX A
UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

CHARLES REYNOLDS and LOIS A. REYNOLDS, his wife, as individuals and as parents and next friends of STEVEN REYNOLDS, and STEVEN REYNOLDS, individually,	)	
Plaintiffs-Appellants,	)	
v.	)	No.79-2068
UNITED STATES OF AMERICA,	)	
Defendant-Appellee.	)	

Appeal From the United States District Court
For the District of New Mexico
(D.C. No. CIV-79-135C)

Richard E. Ransom of Smith, Ransom & Gilstrap Law Offices, Albuquerque, New Mexico, for Plaintiffs-Appellants.

R.E. Thompson, United States Attorney, Albuquerque, New Mexico, for Defendant-Appellee.

Before BARRETT, DOYLE and SEYMOUR, Circuit Judges.

BARRETT, Circuit Judge.

Charles Reynolds and Lois A. Reynolds, his wife, as individuals and as parents and next friends of Steven Reynolds, a minor, appeal from an order granting the defendant United States of America's motion for judgment on the pleadings for failure to state a claim upon which relief can be granted.

Well Pleaded Facts

Inasmuch as this appeal is from the grant of a Rule 12(b)(6) motion, we must accept as true the material facts alleged in Reynolds' First Amended Complaint. *Hospital Building Co. v. Rex Hospital Trustees,* 425 U.S. 738, 740 (1976).

Armond and Renee Fourton, who reside in rural Taos County, New Mexico, applied for and received financial assistance through the Farmers Home Administration (FmHA), Department of Agriculture, United States of America, to construct a residence on their farm property (the FmHA is an agency of the United States); Tom Ramsey, the Taos County Supervisor for the FmHA, in conjunction with the office of the New Mexico State Director, David W. King, approved the construction and/or permanent mortgage arrangements submitted by the Fourtons; during construction of the Fourton residence, the building contractor installed a heating system equipped by the manufacturer for use of natural gas; during the course of construction and prior to occupancy of the residence on June 14, 1976, the FmHA had inspected the residence and the quality and safety of its construction; about November 1, 1976, the Fourtons departed their new residence for two weeks during which time they arranged for Steven Reynolds to spend his evenings in the home for purpose of its safekeeping; on November 5, 1976, Steven Reynolds was asphyxiated and poisoned by carbon monoxide by reason of the negligent installation of the heating system which was connected to a supply of butane, contrary to the [furnace] manufacturer's specification; the furnace heating system was unsafe as installed, but the FmHA County Inspector, acting pursuant to the mortgage loan, inspected and approved the Fourton residence and the Fourtons relied on the approval; during the construction and/or inspection the FmHA, acting pursuant to it mortgage loan, either unreasonably inspected or failed to inspect the furnace system and this unreasonable conduct caused Steven Reynolds' severe and permanent brain damage and severe and permanent physical paralysis; FmHA should have reasonably anticipated a third person invitee's presence at the Fourton residence; Charles Reynolds and his wife, Lois, have incurred and will incur medical expenses and hospital expenses, as the parents and natural guardians of Steven Reynolds,

and have suffered other monetary damages and mental anguish as a direct and proximate result of the FmHA's negligent acts and omissions.

Trial Court Order

The District Court granted the defendant United States of America's motion for judgment on the pleadings following review and consideration of all pleadings and memoranda of the parties.[1] The Court concluded ". . . that Defendant, through the Farmers Home Administration, owed no duty to inspect for safety to Plaintiff and is, therefore, not liable to Plaintiff as a matter of law;" [R., Vol. I, p. 11].

Issues on Appeal

The issues presented for our review are whether the United States of America, through the FmHA, owed a tort duty of ordinary care to its borrowers' (Fourtons) invitee (Steven Reynolds) to inspect for and disapprove unsafe conditions existing in the residential structure pursuant to FmHA mortgage loan procedures, and [per Government's brief] whether the "misrepresentation" exception of the Federal Tort Claims Act bars the recovery sought by Reynolds.

Discussion

Reynolds brought this action under the Federal Tort Claims Act, 28 U.S.C. § 2674, which provides that the United States shall be liable to tort claimants in the same manner as a private individual under similar circumstances. Jurisdiction in the District Court rested on 28 U.S.C. § 1346(b) which permits suit against the United States:

> . . . for injury or loss of property . . . caused by the negligent or wrongful act or omission of any employee of the Government while acting within the scope of his office or employment, under circumstances where the United States, if a private person, would be liable to the claimant in accordance with the law of the place where the act or omission occurred.

Thus, Reynolds contend that the issue is whether the material allegations contained in the First Amended Complaint are legally sufficient to state a claim for relief against a private individual. In sup-

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[1]While denominated a judgment on the pleadings, dismissal of the complaint lies under Fed. Rules Civ. Proc. rule 12(b)(6), 28 U.S.C. because no answer to the complaint was filed.

port thereof, Reynolds rely on Section 324A of the Restatement, Second, Torts (1965) relating to liability to third persons for negligent performance of an undertaking:

> One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of a third person or his things, is subject to liability to the third person for physical harm resulting from his failure to exercise reasonable care to protect his undertaking, if
>
> (a) his failure to exercise reasonable care increases the risk of such harm, or
>
> (b) he has undertaken to perform a duty owed by the other to the third person, or
>
> (c) the harm is suffered because of reliance of the other or the third person upon the undertaking.

In *Moya v. Warren*, 544 p.2d 280 (N.M. Ct. App. 1975), the Court recognized the applicability of § 324A, *supra*, in federal tort claim suits involving contractual obligations. In that case, the plaintiff was in the position of a third person. The Court held the defendant owed no duty to the plaintiff, and relied on the well-established rule that in any tort action it is incumbent upon the plaintiff to establish the defendant owed a duty to plaintiff and that the defendant failed to observe the standard of care which the law requires in the performance of that duty.

Neither 28 U.S.C. § 2674 (the Federal Tort Claims Act) or 28 U.S.C.A. § 1346(h) provide an independent cause of action. These statutes simply waive the sovereign immunity of the United States and render the Government liable to the same extent as a private individual under like circumstances. No recovery may be had under the Federal Tort Claims Act by virtue of specific exceptions carved out under 28 U.S.C. § 2680, including any claim arising out of *misrepresentation*. The District Court did not rule that the "misrepresentation" exception applied. Instead, the Court granted judgment predicated on the proposition that the FmHA owed no tort duty of ordinary care to the safety of its borrowers' invitee.

On appeal, the Government argues that the District Court correctly found that the Government owed no tort duty to the plaintiffs. In addition, the Government contends that the "misrepresentation" excep-

tion of the Tort Claims Act applies and thus bars the claim.

The Housing Act of 1949

Before discussing our disposition of the appeal, we will review the Housing Act of 1949, as amended, in order to probe the nature of the Government's duty involved in the case at bar, and to determine whether the Act provides a basis for recovery based upon Reynolds' First Amended Complaint. In considering these matters, we note that an appellate court may affirm a district court judgement on a basis not relied on by the district court if supported by the record and the law. In *Pound v. Insurance Company of North America*, 439 F.2d 1059 (10th Cir. 1971) we said: ". . . we are reminded of our well established appellate maxim that if a trial court's decision is correct upon any proper theory, we will uphold that decision . . ." 439 F.2d at p. 1062. *See also*: *Coleman v. Mountain Mesa Uranium Corp.*, 240 F.2d 12 (10th Cir. 1956); 10 Wright and Miller, Federal Practice and Procedure, § 2716, pp. 439-441.

The primary congressional purpose underlying the enactment of the Housing Act of 1949, as amended, is "the realization as soon as feasible of the goal of a decent home and a suitable living environment for every American family . . . " 42 U.S.C. § 1441 (1970). Title V of the Act declares that such a goal is to be sought for farm families and others living in rural areas who are unable to obtain credit to secure decent housing. It seeks to remedy that condition by extending financial assistance to such persons through loans authorized by the Secretary of Agriculture. 42 U.S.C. § 1471, *et. seq.* Section 502 of the Act authorizes loans if the Secretary determines that the qualified applicants have the ability to repay them in full, with interest, based upon the income and earning capacity of the applicant and his family from the farm and other sources. 42 U.S.C. § 1472(a). The Act specifically declares that the financial assistance authorized is designed to ". . . enable them to construct, improve, alter, repair or replace dwellings and other farm buildings . . . in order to provide them, their tenants, lessees, sharecroppers, and laborers with decent, safe and sanitary living conditions and adequate farm buildings . . ." 42 U.S.C. § 1471(a)(1).

7 CFR 1802.2(b) reiterates that the primary objectives of FmHA assistance are to achieve the aforesaid stated objectives of the loan and to protect the interests of the government [7 CFR 1822.7(a)] while

assisting such families to obtain decent, safe, and sanitary housing. Other significant, relevant regulations are:

> 7 CFR 1804.3(d)(1) which provides:
>
> . . . All new buildings to be constructed and all alterations and repairs to buildings will be planned to conform with good construction practices. All improvements to the property will conform to applicable laws, ordinances, codes, and regulations which relate to safety and the sanitation of buildings.
>
> 7 CFR 1804.4(g)(3), which provides:
>
> . . . The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with the plans and specifications. He will make a final inspection at the earliest possible date after completion of the planned development. When several major items are involved, he will make final inspections upon completion of each item.

7 CFR 1804.4 (g)(3)(i)(a), (b) and (c) provides that the local county supervisor should make inspections at three specific stages of construction and at such other stages as the county supervisor determines proper. The final stage is identified as "When all onsite and offsite development of the structure has been completed and ready for occupancy."

In the entire scheme, the inspection procedures and approval of the construction by the FmHA precede and are conditions precedent to loan closing and occupancy.

Our Disposition

In *United States v. Neustadt*, 366 U.S. 696 (1961) the Supreme Court held that a home purchaser's claim against the United States for damages resulting from the purchaser's reliance on an inaccurate FHA inspection and appraisal constituted a claim of misrepresentation within the meaning of 28 U.S.C. § 2680(h) and thus not actionable against the United States.

The owner of the residence, as seller, had secured an FHA inspection and appraisal in order to insure the availability of FHA mortgage insurance to purchasers who desired to employ that avenue of financing. The FHA inspection-appraisal did not disclose any defects in the structure disqualifying it for mortgage insurance. The purchaser ac-

quired the property on a conditional sales contract for $24,000.00 in reliance on the FHA appraisal of $22,750.00. A FHA insured mortgage was obtained by the purchaser.

Following the transaction, the purchaser discovered material defects in the structure. He filed suit against the United States under the Federal Tort Claims Act for the difference between the fair market value of the property and the $24,000.00 purchase price, alleging that the FHA was negligent in conducting the inspection and appraisal.

Of particular significance here, the *Neustadt* Court observed that in all such instances, the government may be said to owe a "specific duty" to obtain and communicate information carefully in order to avoid misleading the intended recipient to his financial harm. However, even though the Court was critical of carelessness by government personnel in performing such functions, still it reasoned that the plain words employed by Congress in limiting the scope of governmental tort liability could not be ignored. The Court squarely held that the "misrepresentation" exception of 28 U.S.C. § 2680(h) applied to the negligent, faulty appraisal which was, of course, predicated on the negligent inspection. The Court states that Congress did not intend to convert the FHA appraisal into a warranty of value or otherwise extend to a purchaser any actionable redress by reason of negligent inspection-appraisal.

In addition to *United States v. Neustadt, supra*, "misrepresentation" exception of 28 U.S.C § 2680(h) has been applied in similar cases involving federal housing programs under circumstances where government employees were found to have practiced false representations which worked to the financial detriment of parties who properly relied thereon. *Moon v. Takisaki*, 501 F.2d 389 (9th Cir. 1974); *United States v. Longo*, 464 F.2d 913 (8th Cir. 1972); *Thompson v. United States*, 408 F.2d 1075 (8th Cir. 1969); *Edelman v. Federal Housing Administration*, 382 F.2d 594 (2d Cir. 1967); *Stanley v. Veterans Administration*, 454 F.Supp. 9 (E.D. Pa. 1978); *Modular Technics Corp. v. South Haven Houses Housing Development Fund Co.*, 403 F.Supp. 204 (D. N.Y. 1975); *United States v. Chelsea Towers, Inc.*, 295 F.Supp. 1242 (D.N.J. 1967); *United States v. Sherman Gardens Company*, 298 F.Supp. 1332 (D. Nev. 1967); *United States v. Lawrence Towers, Inc.*, 236 F.Supp. 208 (E.D. N.Y. 1964).

In *United States v. Neustadt, supra*, the Court observed:

> To say, as the Fourth Circuit did, that a claim arises out of "negligence", rather than "misrepresentation", when the loss suffered by the injured party is caused by a breach of a "specific duty" owed by the Government to him, *i.e.*, the duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely in the conduct of his economic affairs, is only to state the traditional and commonly understood legal definition of the tort of "negligent misrepresentation", as is clearly, if not conclusively, shown by the authorities set forth in the margin, and which there is every reason to believe Congress had in mind when it placed the word "misrepresentation" before the word "deceit" in § 2680(h). As the Second Circuit observed in *Jones v. United States, supra*, "deceit" alone would have been sufficient had Congress intended only to except deliberately false representations.
>
> 366 U.S. at pp. 706, 707.

The "misrepresentation" exception of 28 U.S.C. § 2680(h) has been broadly construed to include false representations of any type. In *Hall v. United States*, 274 F.2d 69 (10th Cir. 1959), suit was brought by owners of livestock alleging that federal agents engaged in testing livestock for brucellosis negligently quarantined the livestock even though they were, in fact, not diseased. The complaint alleged that the livestock owner suffered damages because he was compelled to sell the livestock at less than the fair market value. This Court upheld the trial court's dismissal of the complaint and said:

> We must then look beyond the literal meaning of the language to ascertain the real cause of complaint. Plaintiff's real claim is that because of the negligent manner in which these tests were made, the result showed that plaintiff's cattle were diseased; whereas, in fact, they were free from disease and that the Government misrepresented the true condition of these cattle. Plaintiff's loss came about when the Government agents misrepresented the condition of the cattle, telling him they were diseased when, in fact, they were free from disease. The claim is that this misrepresentation caused plaintiff to sell his cattle at a loss. This stated a cause of action predicated on a misrepresentation. Misrepresentation as used in the exclusionary provision of the Statute was meant to include negligent misrepresentation.
>
> 274 F.2d at p. 71.

In *Cason v. United States*, 381 F.Supp. 1362 (W.D. Mo. 1974) the Court similarly observed.

> Plaintiffs now suggest that their claim for damages under subsection 1346(h) was not based on misrepresentation but simply on the negligence of the FHA in applying and enforcing the appropriate statutes and regulations pertaining to inspections and appraisals. Even on a simple negligence theory plaintiffs have failed to state a claim for which damages could be granted. In order to recover on such a theory, plaintiffs would have to demonstrate that a duty of due care was owed plaintiffs by the FHA in the application and enforcement of the statutes and regulations in question. It is now settled, however, that the primary and predominant objective of the FHA appraisal system is the protection of the Government and its insurance funds; that the mortgage insurance programs do not insure anything other than the repayment of loans made by lender-mortgagees; "and that 'there is no legal relationship between the FHA and the individual mortgagor.' " *United States v. Neustadt, supra*, 366 U.S. at 709, 81 S.Ct. at 1301. Although *Neustadt* was based on a different theory of liability, the Court believes that the Supreme Court completely rejected the notion that Congress intended to establish a duty of due care for the benefit of mortgagors such as plaintiffs. *See Jackson v. Romney*, 355 F.Supp. 737, 741-743 (D.D.C. 1973); *cf. Davis v. Romney*, 490 F.2d 1360, 1371-1372 (3d Cir. 1974). In the absence of such a duty, plaintiffs cannot recover damages under a negligence theory.
>
> 381 F.Supp. at p. 1367.

We must hold that the claim asserted by the plaintiffs-appellants in the instant case arises out of misrepresentation by the FmHA and is, accordingly, not actionable under the "misrepresentation" exception contained in § 2680(h) of the Federal Tort Claims Act. *Accord: Irzyk v. United States*, 412 F.2d 749 (10th Cir. 1969), where the government was held exempt from liability under § 2680(h) for alleged negligent supervision-inspection of an independent government contractor; *Hall v. United States, supra; Saxton v. United States*, 456 F.2d 1105 (8th Cir. 1972), where government was held exempt under 28 U.S.C. § 2680(h) by reason of negligent representation that cattle tested were not diseased; *Anglo-American and Overseas Corporation v. United States*, 242 F.2d 236 (2d Cir. 1957), where government was held exempt under § 2680(h) for negligent misrepresentation following F.D.A. inspection of unpure tomato paste; *Clark v. United States*, 218 F.2d 446 (9th Cir. 1954), where government was held exempt by § 2680(h) for alleged misrepresentation that a housing project was safe from flood; *Adamsville Lumber Company v. Rainey*, 348 F.Supp. 373 (W.D. Tenn. 1972), where government held exempt under § 2680(h) for alleged FHA misrepresentation to lumber company relative to home purchase being properly insured; *Marival, Inc. v. Planes, Inc.*, 306 F.Supp. 855 (N.D. Ga. 1969), where government was held exempt

under § 2680(h) where inspector negligently inspected and certified an airplane's airworthiness; and *Feffer v. United States*, 166 Ct. Cl. 506 (1964), where government held exempt under § 2680(h) for erroneous information given by a U.S.D.A. inspector as to temperature at which viability of seed would be affected.

Finally, we observe that sovereign immunity waivers are strictly construed. *Hurley v. United States*, 624 F.2d 93 (10th Cir. 1980). The United States, as sovereign, may not be sued without its consent and the terms of its consent to be sued define the Court's jurisdiction. *United States v. Sherwood*, 312 U.S. 584 (1941); *Buck v. United States*, 466 F.2d 481 (10th Cir. 1972). In *Cort v. Ash*, 422 U.S. 66, 84 (1975), the Supreme Court stated that while it is the duty of the courts to provide such remedies as are necessary to make effective the congressional purpose, the courts must guard that the remedy sought would aid the primary congressional goal.

WE AFFIRM.

APPENDIX B

No. 80-1278

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

ONILEA NEAL,
Plaintiff-Appellant,

v.

ROBERT BERGLAND, ET AL.,
Defendants-Appellees.

APPEAL from the United States District Court, Eastern District of Tennnessee.

Decided and Filed May 1, 1981.

Before: MERRITT and MARTIN, Circuit Judges; COHN, District Judge.*

I.

COHN, District Judge. Plaintiff appeals from a dismissal of her action against Robert Bergland, Secretary of Agriculture, and others,[1] for failure to state a claim upon which relief can be granted and for lack of subject matter jurisdiction. The District Court, in a decision reported at 489 F. Supp. 512

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* Honorable Avern Cohn, United States District Judge, Eastern District of Michigan, sitting by designation.

[1] Other defendants are Gordon Cavanaugh, Administrator of the Farmers Home Administration; Earl Wayne Avery, Tennessee State Director of the Farmers Home Administration; S. Lane Parkison, Roane County Supervisor of the Farmers Home Administration; Mary C. Wells, Assistant Roane County Supervisor of the Farmers Home Administration; Home Marketing Associates, Inc., a construction company; and C. E. Scott, Jr., Gary Humphreys and Wayne Humphreys, employees of or doing business as Home Marketing Associates, Inc.

(E.D. Tenn. 1980), held that neither Title V of the Housing Act of 1949 (the Act), 42 U.S.C. § 1471 *et seq.*, nor regulations issued thereunder, 7 C.F.R. § 1802.71 *et seq.*, create an obligation on the part of the Farmers Home Administration (FmHA)[2] to supervise, inspect or warrant the construction of the prefabricated house built for plaintiff by defendant Home Marketing Associates (Home Marketing) and financed by FmHA.

For the reasons that follow we reverse and remand for further proceedings.

II.

Plaintiff is an unmarried woman in her mid-fifties with less than a high school education. She has never before owned a home. After an unsuccessful attempt to find housing to rent or purchase within her financial means, plaintiff applied for and received a direct rural housing loan from FmHA in 1976.

Plaintiff then consulted with defendant Parkison and entered into a construction contract with defendant Home Marketing for the construction of a prefabricated house. The contract provided that construction conform to FmHA approved plans; that changes in the plans be made only with the written approval of FmHA; and that FmHA have the right to inspect or test all materials and workmanship and reject any that were defective.

During the course of construction, defendant Wells conducted inspections of the house when it was 2% complete, 99% complete and 100% complete. There were no notes or comments in any of her inspection reports indicating any condition at variance with the approved plans and specifications.

Upon completion of construction, defendant Home Market-

---

[2] FmHA is an agency of the Department of Agriculture authorized by § 502 of Title V of the Housing Act of 1949, 42 U.S.C. § 1472, to extend financial assistance in home construction and purchase to persons of low to moderate income residing in rural areas.

ing issued plaintiff a one year builder's warranty as required by FmHA, which represented construction was in conformance with the drawings and specifications approved by FmHA and the minimum property standards published by the Department of Housing and Urban Development. The warranty covered workmanship, materials and equipment including the heating system.

In December 1977 plaintiff notified FmHA and defendant Home Marketing that the heat pump in her house was not working properly. Defendant Avery and other FmHA officials inspected the house and notified defendant Home Marketing of thirteen defects, including the heat pump, which needed correction. Defendant Home Marketing failed to cure the defects.

In November 1978 plaintiff asked FmHA to pay for correcting the heating system and other construction defects. It declined. After exhausting her administrative remedies, 28 U.S.C. § 2675, plaintiff brought this suit.

III.

The case was started in the Circuit Court of Roane County, Tennessee and thereafter removed to the United States District Court for the Eastern District of Tennessee by defendant Bergland. 28 U.S.C. § 1441.

In her amended complaint plaintiff alleged a breach of contract by FmHA for failure to provide technical assistance including inspection and supervision of construction of the house; negligence for failure to properly execute its obligation to inspect and supervise construction of the house; and detrimental reliance for failure to perform its regulatory obligations as promised. Plaintiff also sought mandamus to compel defendant Bergland to compensate her for the construction defects in the house under Section 509 of the Act, 42 U.S.C. § 1479(c).[3]

[3] At oral argument plaintiff represented defendant had satisfied this request thereby mooting this issue.

In essence, plaintiff alleged the Act and the regulations under it created an obligation on the part of FmHA to supervise construction of the house to ensure compliance with the purpose of the FmHA loan program which the Act recites is for rural residents to obtain "decent, safe, and sanitary living conditions . . . ." 42 U.S.C. § 1471(a).

The District Court rejected plaintiff's claims and remanded the case to the state court holding there is no duty owed plaintiff by FmHA under the Act since the purpose of the rural housing loan program is limited to providing participants with an opportunity to obtain decent housing and not to make the government "an insurer of the quality of the workmanship or structures funded with the loan proceeds." 489 F. Supp. at 514. The District Court equated FmHA's position with that of a mortgagee and looked at supervision of construction authorized by the regulations as a means of protecting FmHA's security interest in the mortgaged property.

> "To hold the FmHA liable for the shoddy work of the contractor would be tantamount to making a mortgagee the warrantor of the quality of its security."

489 F. Supp. at 515.

IV.

A.

The Secretary of Agriculture is authorized by § 502 of the Act, 42 U.S.C. § 1472, to extend financial and technical assistance, through FmHA, to eligible rural residents to enable them to obtain "decent, safe, and sanitary" housing. 42 U.S.C. § 1471(a). The regulations state,

> "The basic objective of the Farmers Home Administration (FmHA) in making section 502 loans is to assist farmowners and other persons who will live in rural areas to obtain decent, safe, and sanitary dwellings and related facilities. The purpose of these loans it to give families,

> who do not have sufficient resources to provide such dwellings and related facilities on their own account and cannot obtain the necessary credit from other sources on terms and conditions they reasonably can be expected to meet, an opportunity to have adequate homes."

7 C.F.R. § 1822.2.

FmHA is authorized to provide financial assistance either by direct loans through the Secretary of Agriculture pursuant to section 502 of the Act, 42 U.S.C. § 1472, or by insured or guaranteed loans pursuant to section 517 of the Act, 42 U.S.C. § 1487, and the regulations, 7 C.F.R. § 1841.46 *et seq.*

Although Title V focuses on financial assistance, S. Rep. No. 84, 81st Cong., 1st Sess. 2, *reprinted in* [1949] U.S. Code Cong. Serv. 1550, 1576, Congress has also provided for research and technical services "pointed toward more efficient and more economical construction" of houses and related structures. *Id.* Section 506 of the Act provides,

> "Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition to the financial assistance authorized . . . *the Secretary is authorized to furnish . . . technical services such as building plans, specifications, construction supervision and inspection . . . .*"

42 U.S.C. § 1476(a) (emphasis added).

The regulations provide:

> "Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government . . . ."

7 C.F.R. § 1822.7(a).

Thus while it may be said that the overall objective of the loan program is to provide rural residents an opportunity for

decent, safe, and sanitary housing, it is to be noted that Congress has specifically authorized FmHA to provide technical assistance and supervision of construction.

B.

Plaintiff's contract claim turns on the nature and extent of FmHA's obligation, if any, to provide technical assistance and to inspect and supervise construction. To find FmHA had a contractual obligation it must be expressly provided for either in the Act, the regulations, or the loan papers, or it must be implied in fact from the circumstances surrounding plaintiff's dealings with FmHA, since there can be no right of action against the United States for a contract implied in law. 28 U.S.C. § 1346;[4] *Goodyear Tire & Rubber Co.* v. *United States*, 276 U.S. 287, 293 (1928).

There is no allegation that FmHA expressly promised to provide assistance and neither in the Act nor the regulations is there an explicit obligation on the part of FmHA to inspect or supervise construction for plaintiff's benefit. The right to inspect, without more does not imply an obligation to inspect. *Kaminer Construction Corp.* v. *United States*, 488 F.2d 980 (Ct. Cl. 1973).

Section 506 of the Act, 42 U.S.C. § 1476(a), authorizes the Secretary of Agriculture to furnish a borrower technical services; the regulations governing rural housing loans, 7 C.F.R. § 1822.7, provide that such assistance will be rendered "to

---

[4] The Tucker Act, 28 U.S.C. § 1346, governs contract actions against the United States. It provides,

> "(a) The district courts shall have original jurisdiction, concurrent with the Court of Claims, of:
>
> * * *
>
> (2) Any other civil action or claim against the United States, not exceeding $10,000 in amount, founded . . . upon any express or implied contract with the United States . . . ."

This section acts as a waiver of sovereign immunity and therefore allows the United States to be sued in contract. *Tempel* v. *United States*, 248 U.S. 121, 129 (1918); *National Bank of Newark* v. *United States*, 357 F.2d 704, 706 (Ct. Cl. 1966).

the extent necessary" to achieve the loan objectives; 7 C.F.R. § 1804.4(g)(3), governing planning and performing development work, provides that inspections will be made "as frequently as necessary to assure that construction and land development conforms with the plans and specification"; and 7 C.F.R. § 1802.73 and § 1802.74, governing supervision of borrowers, provide for "supervision necessary to accomplish the objectives of the loan," with emphasis given to, *inter alia*, maintaining the security and protecting the interest of FmHA. Borrowers are to be supervised "to the extent necesary to assure . . . protection of the FmHA's financial interest." 7 C.F.R. § 1802.74. None of these provisions include a clearly defined obligation on the part of FmHA running to plaintiff to perform any supervisory function, but instead speak in terms of discretion on the part of FmHA to render such assistance as it deems necessary to achieve the objectives of the loan program and for the protection of its security interest.

We find that no contractual obligation existed on the part of FmHA to provide technical assistance or to supervise construction or to inspect.

See Ramsey v. *Farmers Home Administration*, 443 F.Supp. 760 (E.D. Mo. 1978); *Adamsville Lumber Co., Inc.* v. *Rainey*, 348 F. Supp. 373 (W.D. Tenn. 1972); *Forcum-Lannon, Inc.* v. *Berry*, 344 F. Supp. 774, (W.D. Tenn. 1972).

C.

Plaintiff's tort claim, however, is on firmer ground; namely the principle expressed in § 323 of the RESTATEMENT (SECOND) OF TORTS (1965)[5] that one who undertakes to

[5] RESTATEMENT (SECOND) OF TORTS § 323 provides:

"One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertaking, if

(a) his failure to exercise such care increases the risk of such harm, or

(b) the harm is suffered because of the other's reliance upon the undertaking."

act, even though gratuitously, is required to act carefully and with the exercise of due care and will be liable for injuries proximately caused by failure to use such care. The Federal Tort Claims Act, 28 U.S.C. § 2671 *et seq.*, authorizes suit against the United States for this kind of claim since the act constitutes a waiver by the United States of its immunity from liability in tort for the acts of its employees and representatives. *Reminga* v. *United States*, 631 F.2d 449 (6th Cir. 1980); Annot., 30 A.L.R. Fed. 421, 430 (1976). This act makes the United States liable, with certain exceptions, 28 U.S.C. § 2680, for the negligence of its employees "in the same manner and to the same extent as a private individual under like circumstances . . . ." 28 U.S.C. § 2674.

The principle expressed in the Restatement is not new, *Erie R. Co.* v. *Stewart*, 40 F.2d 855 (6th Cir. 1930), and has been applied in a number of situations in which a government agency performed the undertaking. *Ingham* v. *Eastern Air Lines, Inc.*, 373 F.2d 227 (2d Cir.), *cert. denied*, 389 U.S. 931 (1967), for example, deals with a negligent act occurring in the operation of the federal air traffic control system.

> "It is now well established that when the government undertakes to perform services, which in the absence of specific legislation would not be required, it will, nevertheless, be liable if these activities are performed negligently. Thus, for example, though the government may be under no obligation in the absence of statute to render medical care to discharged veterans, when it decides to provide such services and does so negligently, it has been held liable under the Tort Claims Act. *United States* v. *Brown*, 348 U.S. 110, 75 S.Ct. 141, 99 L.Ed. 139 (1954)."

373 F.2d at 236.

In *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955), this principle was applied to the Coast Guard in a situation where it was charged with failure to maintain the beacon

lamp in a lighthouse resulting in damage to a barge that went aground. The Supreme Court said that while the Coast Guard need not have undertaken the lighthouse service, once it exercised its discretion to operate the light, thereby engendering reliance on the guidance afforded by the light, it was obligated to use due care to maintain the light and to make repairs or give warnings when the light was not functioning. For failure to do so it was liable in money damages for any injury which resulted.

The government has been held liable for the negligence of its employees in the way they put out a forest fire, *Rayonier, Inc.* v. *United States*, 352 U.S. 315 (1957); for the negligent design and construction of a drainage ditch which caused damage to a railroad, *Seaboard Coast Line Railroad Co.* v. *United States*, 473 F.2d 714 (5th Cir. 1973); for negligence of the Coast Guard in undertaking a rescue operation, *United States* v. *DeVane*, 306 F.2d 182 (5th Cir. 1962); for negligence in inaccurately marking the location of a wrecked ship, *Somerset Seafood Co.* v. *United States*, 193 F.2d 631 (4th Cir. 1951); and for negligence in failing to require a subcontractor to comply with a contract's safety requirements, *Barron* v. *United States*, 473 F. Supp. 1077 (D. Hawaii 1979).

V.

Where claims for negligence against the government have been barred by the Federal Tort Claims Act, *United States* v. *Neustadt*, 366 U.S. 696 (1961) and its progeny, circumstances different than the case at bar were involved.

In *Neustadt*, plaintiffs purchased a house with a private mortgage loan insured by the Federal Housing Administration (FHA) pursuant to § 203 of the National Housing Act of 1934, 12 U.S.C. § 1709. In determining whether the house was eligible for FHA mortgage insurance, the FHA made an inspection and assigned an appraised value to establish the maximum amount of mortgage insurance obtainable. 24 C.F.R. §§ 200.140 - 200.152. FHA found no defects in the

house and issued an insurance commitment. Pursuant to § 226 of the National Housing Act of 1934, 12 U.S.C. § 1715q, the seller provided plaintiffs with a copy of the appraisal report.

Shortly after plaintiffs took possession, the foundation of the house began to shift causing substantial damage to interior and exterior walls. Plaintiffs sued FHA claiming it negligently inspected and appraised the house. Plaintiffs sought recovery of the difference between the fair market value and the purchase price paid claiming they relied on the excessive FHA appraisal.

The Supreme Court denied plaintiff's recovery on the grounds the purpose of the FHA appraisal program is the "'protection of the Government and its insurance funds'", 366 U.S. at 709, and that any tort committed by FHA because of an inaccurate report resulting from negligent inspection of the house, would be one "arising out of . . . misrepresentation" a specie of claims which is specifically excluded from coverage by the Federal Tort Claims Act, 26 U.S.C. § 2680 (h).[6]

> "[T]he duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely in the conduct of his economical affairs, is only to state the traditional and commonly understood legal definition of the tort of 'negligent misrepresentation' . . . ."

366 U.S. at 706. *See also United States* v. *Laurence Towers, Inc.*, 236 F. Supp. 208 (E.D.N.Y. 1964).

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[6] "The provisions of this chapter and section 1346(b) of this title shall not apply to —

• • •

(h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit or interference with contract rights . . . ."

28 U.S.C. § 2680(h).

Examples of *Neustadt* type situations are *Green* v. *United States,* 629 F.2d 581 (9th Cir. 1980), involving a suit by cattle owners against the United States for losses sustained from the application of DDT to cattle grazing land and the failure to adequately warn of the consequences of the chemical; *Preston* v. *United States,* 596 F.2d 232 (7th Cir. 1979), involving a suit by farmers against the United States for losses sustained as a result of storing grain in a warehouse approved by the Department of Agriculture which went bankrupt; and *Marival, Inc.* v. *Planes, Inc.,* 306 F. Supp. 855 (N.D. Ga. 1969), involving a third-party action by the seller of an airplane against the United States for the negligent certification of airworthiness of the airplane given by the Federal Aviation Administration which caused the seller to misrepresent the condition of the plane to the buyer.

Cases distinguishing *Neustadt* illustrate the difference between the application of the Federal Tort Claims Act to a situation dealing with a cause of action based on misrepresentation and a cause of action based on negligent performance of an operational task. In *Ware* v. *United States,* 626 F.2d 1278 (5th Cir. 1980), the negligent misrepresentation exception was held inapplicable to a suit by a farmer against the United States for losses sustained when the Government destroyed his cattle after the Department of Agriculture negligently misdiagnosed them as tubercular.

> "The government's misrepresentation caused Ware to do nothing save remain in ignorance that he had suffered a compensable loss. The government not Ware, destroyed the cattle and caused the damage. Ware's complaint, thus, arose out of, not a negligent misrepresentation, but an allegedly negligent misdiagnosis that caused the government to destroy his cattle."

626 F.2d 1283.

In *In Re Air Crash Disaster Near Silver Plume Colo.,* 445 F. Supp. 384 (D. Kan. 1977), there was a claim of negli-

gent failure on the part of a government employee to perform an operational duty to properly inspect an aircraft. The District Court held,

> "It is the inspection undertaken to protect air travelers from certain dangers which is relied upon by such travelers and which, if negligently performed, gives rise to the very dangers the inspection was intended to prevent. The certification is a reporting of results of such inspection but was not in itself relied upon by plaintiffs in any economic affairs."

445 F. Supp. at 409.

VI.

Plaintiff's claim, as we read it, is based not on misrepresentation, as in the issuance of a false or inaccurate appraisal report, but rather on FmHA's failure to use due care in a voluntary undertaking, i.e., inspection and supervision of the construction of her house. Congress, we believe, intended plaintiff to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the Act and plaintiff's particular circumstances.

The Supreme Court in *Neustadt* noted the distinction we make that its decision "neither conflicts with nor impairs" the authority of *Indian Towing Co.* v. *United States, supra,* saying:

> "As Dean Prosser has observed, many familiar forms of negligent conduct may be said to involve an element of 'misrepresentation,' in the generic sense of that word, but '[s]o far as misrepresentation has been treated as giving rise in and of itself to a distinct cause of action in tort, it has been identified with the common law action of deceit,' and has been confined 'very largely to the invasion of interests of a financial or commercial character, in the course of business dealings.' Prosser, Torts, § 85,

'Remedies for Misrepresentation,' at 702-703 (1941 ed.). See also 2 Harper and James, Tort, § 29.13, at 1655 (1956)."

366 U.S. at 711, n. 26.

There is nothing in the amended complaint or in the facts and circumstances here present which lead to the conclusion that the kind of misrepresentation, as was found in *Neustadt* and as is specifically excluded under § 2680(h) of the Federal Tort Claims Act, is the basis of plaintiff's claim. What plaintiff is complaining of is that FmHA negligently supervised construction and negligently inspected her house.

VII.

The District Court erred in dismissing the amended complaint. It does not appear beyond doubt "that plaintiff can prove no set of facts in suport of [her] claim which would entitle [her] to relief." *Conley* v. *Gibson*, 355 U.S. 41, 45 (1957). The judgment of the District Court is REVERSED and this cause REMANDED to the District Court for further proceedings consistent with this opinion.[7]

[7] Subsequent to the decision in this case the Court of Appeals for the Tenth Circuit released its opinion in *Reynolds, et al.* v. *United States*, No. 79-2068 (filed March 9, 1981), which appears to be contrary to our holding above. Careful review suggests that we take a different view of Congressional intent and the purposes of the statute with regard to technical assistance. Here, unlike *Reynolds*, the damages claimed were the direct consequences of the alleged negligent inspections, i.e., defects in the house. We are satisfied that plaintiff is entitled to go forward with her case.

Office-Supreme Court, U.S.
FILED
AUG 5 1981
ALEXANDER L. STEVAS,
CLERK

No. 80-2064

In the Supreme Court of the United States

OCTOBER TERM, 1980

CHARLES REYNOLDS AND LOIS A. REYNOLDS, ET AL.,
PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

LAWRENCE G. WALLACE
Acting Solicitor General
Department of Justice
Washington, D.C. 20530
(202) 633-2217

QUESTION PRESENTED

Whether a suit alleging a negligent failure by a Farmers Home Association employee to inspect properly a furnace that caused personal injury is barred by the "misrepresentation exception" to suits allowed against the United States under the Federal Tort Claims Act, 28 U.S.C. 2680(h).

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	4
Conclusion	9
Appendix	1a

TABLE OF AUTHORITIES

Cases:

Ausland v. *United States*, 488 F. Supp. 426	8
Bartie v. *United States*, 216 F. Supp. 10, aff'd, 326 F.2d 754, cert. denied, 379 U.S. 852	6
Clark v. *United States*, 218 F.2d 446	6
Diaz Castro v. *United States*, 451 F. Supp. 959	6
Hall v. *United States*, 274 F.2d 69	8
Hicks v. *United States*, 511 F.2d 407	8
Indian Towing Co. v. *United States*, 350 U.S. 61	8
Lloyd v. *Cessna Aircraft Co.*, 429 F. Supp. 181	6
National Manufacturing Co. v. *United States*, 210 F.2d 263, cert. denied, 347 U.S. 964	5
Neal v. *Bergland*, 646 F.2d 1178, petition for rehearing, No. 80-1278 (filed July 13, 1981)	6, 7, 8
United States v. *Neustadt*, 366 U.S. 696	4-5, 6, 7, 8

Statutes and regulations:

Federal Tort Claims Act:	
28 U.S.C. 2674	3
28 U.S..C 2680	4
28 U.S.C. 2680(h)	3, 7
42 U.S.C. (& Supp. III) 1471(a)	2
42 U.S.C. (& Supp. III) 1472	2
42 U.S.C. (& Supp. III) 1487	2

Statutes and regulations (continued): Page

7 C.F.R.:

Section 1804.4 (1980) 2, 6
Section 1804.4(g)(3) (1980) 2
Section 1822.7(a) 2
Section 1924.9 ..... 2, 3

Miscellaneous:

45 Fed. Reg. (1980):

p. 39789 2
p. 39792 3

Restatment (Second) of Torts (1965) 7

In the Supreme Court of the United States

OCTOBER TERM, 1980

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CHARLES REYNOLDS AND LOIS A. REYNOLDS, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-10) is reported at 643 F.2d 707. The order of the district court (App., *infra*, 1a) is not reported.

JURISDICTION

The judgment of the court of appeals was entered on March 9, 1981. The petition for a writ of certiorari was filed on June 5, 1981. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Farmers Home Administration (FmHA) is the agency authorized by the Secretary of Agriculture to extend financial assistance to eligible rural residents to help them acquire "decent, safe, and sanitary living conditions." 42 U.S.C. (& Supp. III) 1471(a). FmHA may provide this assistance either by direct loans from the Secretary of Agriculture (42 U.S.C. (& Supp. III) 1472) or by insured or guaranteed loans (42 U.S.C. (& Supp. III) 1487).

Regardless of the form of the assistance, FmHA's regulations declare generally that "[s]upervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government." 7 C.F.R. 1822.7(a). Specifically, the regulations in effect at all times relevant to this case provided that (7 C.F.R. 1804.4 (g)(3) (1980)):

> The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with the plans and specifications. He will make a final inspection at the earliest possible date after completion of the planned development.[1]

---

[1] The Department of Agriculture amended the FmHA regulations effective June 12, 1980. 45 Fed. Reg. 39789. Section 1804 was deleted and its substance was reenacted as 7 C.F.R. 1924.9 There was one particularly relevant change made in the regulations. They now provide:

> FmHA's inspections are not to assure the borrower that the house is built in accordance with the plans and specifications. The inspections create or imply no duty or obligation to the particular borrower but are, rather, for the dual purposes of determining that FmHA has adequate security for its loan and enabling FmHA to determine that FmHA is working toward achieving the statutory goal of providing adequate housing.

Approval of construction by the county inspector is a condition precedent to occupancy.

2. Armand and Renee Fourton applied for and received a loan to construct a new residence on their farm land in Taos County, New Mexico. The construction of the house was inspected in accordance with the foregoing regulations by the FmHA's county supervisor. Prior to June 1976, when the Fourtons moved into the new house, the FmHA conducted its final inspection of the completed house and approved the mortgage arrangements submitted by the Fourtons.

In November 1976, petitioner Steven Reynolds was house-sitting for the Fourtons. A natural gas furnace, which was installed during construction, had been connected improperly to a supply of butane gas. This caused carbon monoxide to be discharged into the house. As a consequence, Steven Reynolds suffered carbon monoxide asphyxiation and sustained serious brain damage.

3. On February 9, 1979, petitioners[2] filed the instant action under the Federal Tort Claims Act

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7 C.F.R. 1924.9. The Department of Agriculture explained the change as follows:

> [E]xisting statutes provide for these construction inspections to be conducted by FmHA personnel solely to determine adequacy of the FmHA security. Language other than that contained in the final rule may create legal problems by not properly informing the public as to the purpose of these inspections.

45 Fed. Reg. 39792 (1980). Thus, the new regulations were intended to clarify preexisting law on this issue.

[2] Steven Reynolds sued individually. His parents, Charles Reynolds and Lois Reynolds, sued on his behalf and individually.

(FTCA), 28 U.S.C. 2674, against the United States in the United States District Court for the District of New Mexico. They alleged that their injuries were proximately caused by the negligent inspection of the Fourtons' house by the county inspector for the FmHA. The government filed a motion for judgment on the pleadings, asserting that the cause of action was barred by the "misrepresentation" exception to the FTCA, 28 U.S.C. 2680(h).[3]

The district court granted the government's motion, holding that the FmHA "owed no duty to inspect for safety to Plaintiff and is, therefore, not liable to Plaintiff as a matter of law" (App., *infra*, 1a). The court of appeals affirmed, concluding that the complaint was barred by the "misrepresentation" exception applicable to suits by private individuals against the United States (Pet. App. 6-10). The court reasoned (*id.* at 6-8) that this result was mandated by *United States* v. *Neustadt*, 366 U.S. 696 (1961), and other federal court decisions construing the "misrepresentation" exception (Pet. App. 9-10).

ARGUMENT

The decision of the court of appeals correctly applied the Federal Tort Claims Act's "misrepresentation" exception as interpreted in *United States* v.

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[3] The relevant portion of 28 U.S.C. 2680 provides:

The provisions of this chapter and section 1346(b) of this title shall not apply to—

* * * * *

(h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights * * *.

Neustadt, 366 U.S. 696 (1961). Review by this Court therefore is unwarranted.

1. In *Neustadt*, an inspector for the Federal Housing Administration (FHA) failed to discover cracks in the foundation of a house that was financed by the FHA. Plaintiffs alleged and the court of appeals held that FHA breached a "duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely." 366 U.S. at 706. This Court held that the plaintiffs had alleged only "the traditional and commonly understood * * * tort of 'negligent misrepresentation'" and therefore disallowed their claims. *Ibid.* The Court also rejected the argument that the FHA owed a duty to protect the mortgagor based on the statutory requirement of making an inspection and offering an appraisal. *Id.* at 708. It concluded that those requirements were for the benefit of the government, not the purchaser. *Id.* at 708-709.

Petitioners argue that, unlike *Neustadt*, this case involves the duty to use due care in a safety inspection. This characterization of the issue, however, does not alter the gravamen of petitioners' complaint that the FmHA breached a "duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely." That the effects of the FmHA's actions are concededly more serious than those in *Neustadt* does not affect the basic tort theory underlying the complaint.[4] As the Court stated in *Neustadt*:

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[4] *Neustadt* cited with approval *National Manufacturing Co. v. United States*, 210 F.2d 263 (8th Cir.), cert. denied, 347 U.S. 967 (1954), a case in which the misrepresentation exception was applied to misinformation given by the govern-

> While we do not condone carelessness by government employees in gathering and promulgating such information, neither can we justifiably ignore the plain words Congress has used in limiting the scope of the Government's tort liability.

Id. at 710-711.

Moreover, petitioners cannot avoid the second holding in *Neustadt* that provision for inspection of housing construction by itself does not create any duty on the part of the government to protect the buyer (or, here, the buyer's invitee). Petitioners have made no showing that the Housing Act of 1949 created a duty to assure that an FmHA-financed house is safe. They rely upon references to "safe" housing in the regulations (7 C.F.R. 1804.4 (1980)), but ignore the fact that the stated purpose of government inspections is "to achieve the objective of the loan program and * * * the protection of [the federal government's] security interest." *Neal* v. *Bergland*, 646 F.2d 1178, 1181 (6th Cir. 1981), petition for rehearing,

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ment in the form of flood forecasts that allegedly contributed to physical damage to plaintiffs' goods, wares, and merchandise. *United States* v. *Neustadt*, 366 U.S. at 702-703. See also *Clark* v. *United States*, 218 F.2d 446 (9th Cir. 1954) (government agency that inspected embankment and notified residents that they were safe was not liable when embankment collapsed, causing injury and death). See also *Bartie* v. *United States*, 216 F. Supp. 10, 20-21 (W.D. La. 1963), aff'd, 326 F.2d 754 (5th Cir.), cert. denied, 379 U.S. 852 (1964); accord, *Diaz Castro* v. *United States*, 451 F. Supp. 959 (D. P.R. 1978) (misrepresentation exception applied in case of bodily injury); *Lloyd* v. *Cessna Aircraft Co.*, 429 F. Supp. 181 (E.D. Tenn. 1977) (misrepresentation exception applied in wrongful death action resulting from plane crash).

No. 80-1278 (filed July 13, 1981). It is the developer or builder, not the federal government, who must assume the duty to protect the mortgagor's financial and physical well being.

2. Relying primarily upon the decision of the Sixth Circuit in *Neal* v. *Bergland, supra*, petitioners argue (Pet. 6-7) that there is a conflict among the courts of appeals on the proper application of Section 2680(h). In *Neal*, the court of appeals held that the misrepresentation exception does not bar a suit by a mortgagor against the United States alleging that the FmHA negligently inspected and supervised construction of a house. The Court reasoned that the "good Samaritan" rule described in the *Restatement (Second) of Torts* § 323 (1965)[5] creates a basis for liability that is distinct from negligent misrepresentation. From this premise, the court concluded that a suit based on an alleged breach of a gratuitous duty to inspect was not barred by Section 2680(h).

The error in the Sixth Circuit's analysis is that *Neustadt* by necessary implication rejected the argument that failure by a government agency to in-

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[5] The *Restatment* defines the rule as follows:

> § 323. Negligent Performance of Undertaking to Render Services.
>
> One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertakings, if
>
> (a) his failure to exercise such care increases the risk of such harm, or
>
> (b) the harm is suffered because of the other's reliance upon the undertaking.

spect and disclose defects is actionable under a "good Samaritan" theory despite the misrepresentation exception. The classic illustration of the "good Samaritan" rule is *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955). In that case, the Coast Guard gratuitously operated a lighthouse beacon and negligently allowed it to stop operating. This Court held that the Coast Guard was liable for the injuries it caused. The Court in *Neustadt* distinguished *Indian Towing* on the ground that the activity that caused the injury could not fairly be characterized as a "misrepresentation." See *United States* v. *Neustadt, supra*, 366 U.S. at 711 n.26. In this case, as in *Neal*, the essence of the claim is negligent misrepresentation resulting from the failure of the FmHA to discover and disclose the defect in the building.

We therefore acknowledge the existence of a conflict between the Tenth Circuit's decision in this case and the Sixth Circuit's decision in *Neal*,[8] but submit

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[8] The other cases relied upon by petitioners (Pet. 8) are readily distinguishable on their facts. In each case, the applicability of the misrepresentation exception turned on whether the substance of the plaintiff's claim was reliance on misinformation by the government. See *Hicks* v. *United States*, 511 F.2d 407, 414 (D.C. Cir. 1975) (misrepresentation exception not applied since "basis for the claim" was government's independent responsibility in discharge of dangerous patient from hospital); *Ausland* v. *United States*, 488 F. Supp. 426, 431 (N.D.S.D. 1980) (misrepresentation exception not applied since United States actually sold plaintiffs contaminated grain); *Hall* v. *United States*, 274 F.2d 69, 71 (10th Cir. 1959) (exception applied since gravamen of complaint was that government had given plaintiffs misinformation on health of cattle after Department of Agriculture testing).

that the Sixth Circuit's decision is plainly inconsistent with this Court's decision in *Neustadt*. The government has filed a petition for rehearing en banc in the *Neal* case. Accordingly, there is no need at this time for the Court to resolve the conflict. There will be ample opportunity to decide this issue if the Sixth Circuit should deny the government's petition for rehearing en banc.[7]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

LAWRENCE G. WALLACE
Acting Solicitor General

AUGUST 1981

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[7] We also note that, in light of the clarifying amendments to the regulations regarding FmHA inspections that have been adopted by the Department of Agriculture (see note 1, *supra*), it is doubtful that plaintiffs in the future will file suits against the FmHA claiming that they relied upon its inspections to protect their interests.

APPENDIX

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

No. CIV-79-135 C

CHARLES REYNOLDS and LOIS A. REYNOLDS, his wife, as individuals and as parents and next friends of STEVEN REYNOLDS and STEVEN REYNOLDS, individually, PLAINTIFFS

vs.

UNITED STATES OF AMERICA, DEFENDANT.

Filed Aug. 28, 1979

ORDER

THIS MATTER having come before the Court on Defendant's Motion for Judgment on the Pleadings filed June 15, 1979, and the Court having reviewed the pleadings and memoranda on file and being otherwise fully advised in the premises, concludes that Defendant, through the Farmers Home Administration, owed no duty to inspect for safety to Plaintiff[s] and is, therefore, not liable to Plaintiff[s] as a matter of law;

IT IS, THEREFORE, ORDERED that Defendant's Motion for Judgment on the Pleadings be, and it hereby is, granted.

/s/ Santiago E. Campos
SANTIAGO E. CAMPOS
United States District Judge

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